Dayton Hudson Corporation 1987 Annual Report

Corporate Profile

Dayton Hudson Corporation is a growth company focusing exclusively on retailing. At year-end, the Corporation operated 577 stores in 36 states.

Dayton Hudson's principal strategy is to provide exceptional value to the American consumer through multiple retail formats. Retail operations are conducted by four business segments:

□ **Target** is an upscale discount store chain operating in 24 states. Target offers low prices on a broad assortment of high-quality fashion and basic hardlines and softgoods in easy-to-shop, self-service stores.

□ **Mervyn's** is a highly promotional, popular-priced, value-oriented department store company operating in 13 states. Mervyn's stores feature nationally branded and private-label apparel, accessories and household softgoods.

□ **Dayton Hudson Department Store Company** (DHDSC) emphasizes fashion leadership, quality merchandise, broad selections and customer service. It operates Hudson's and Dayton's stores in seven states.

□ **Lechmere** is a hardlines retail company operating in eight states. Lechmere stores offer products from four distinct worlds of merchandise: consumer electronics, major appliances, housewares and leisure-time equipment.

About the Cover

Mervyn's new prototype store in Dublin, California integrates store design, visual merchandising and merchandise presentation in an effort to make shopping more pleasant and convenient for Mervyn's customers. The design features new graphics, signing and accent lighting. Many of the key elements of the prototype will be incorporated into existing stores.

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Financial Highlights

Continuing Operations

(Millions of Dollars, Except Per Share Data)	1987	1986*	Percent Increase/ (Decrease)
For the Year:			
Revenues	**$10,677.3**	$9,259.1	15%
Net earnings	**228.4**	255.0	(10)
Net earnings per share	**2.41**	2.62	(8)
Cash dividend paid per share	**.92**	.84	10
At Year-End:			
Shares outstanding	**85,775,189**	97,368,703	
Number of shareholders	**16,684**	15,480	
Retail square feet	**57,453,000**	47,672,000	
Number of stores	**577**	475	

*Results for 1986 are before an extraordinary charge and discontinued operations.

The Year in Review

- □ Total revenues topped $10 billion, increasing 15% over the previous year.
- □ Net earnings per share were $2.41, compared with $2.62 a year ago.
- □ A record 104 new stores opened, increasing total retail space by 21% and giving us a presence in some important new markets.
- □ Bruce G. Allbright was elected President and a member of the Board of Directors of Dayton Hudson. Mr. Allbright was previously Chairman and CEO of Target.
- □ Robert J. Ulrich, President and Chief Operating Officer of Target, was named Chairman and CEO of Target.
- □ The Board of Directors authorized the purchase of up to 15 million shares of the Corporation's outstanding stock. At fiscal year-end, we had purchased 11.8 million shares at an average price of $29.
- □ We announced a $600 million capital investment plan for 1988.
- □ We confronted an unsolicited hostile takeover proposal.

Kenneth A. Macke
Chairman of the Board and
Chief Executive Officer

We at Dayton Hudson Corporation are currently operating in a retailing environment of rapid change and unprecedented competition. Many of the challenges we faced in 1987 were brought on by this environment. Importantly, we learned that Dayton Hudson is up to the challenge.

This report aims to share with you what we have achieved, how we intend to improve even further, and where we are going as a Corporation.

Our overriding goal is to achieve consistent earnings growth and a significant return on investment for our shareholders. We are not pleased with the results for 1987. We are encouraged that the changes we made in recent years had a positive effect on fourth-quarter results. We believe that our 1988 results will reflect continuing progress.

We are determined to get back to our historical record of consistent, strong earnings growth. We know that in order to achieve this goal we must balance our long-term investments and our near-term performance.

That is what we have been working toward.

□ We have made substantial improvements at Mervyn's to make it more responsive to customers. We implemented an aggressive program to improve merchandise values by raising quality standards and reducing prices. Customers and industry observers are responding positively, with considerable excitement about these changes.

□ Target has made a major strategic thrust into California while turning in its 13th consecutive year of record earnings.

□ All of our companies have made a major investment in new technology designed to make shopping easier, more convenient and more responsive to customer needs and desires. New programs are underway to improve the flow of merchandise from manufacturers to customers.

□ We have invested heavily in innovative retailing concepts in each of our companies and expanded our proven retailing formats to capitalize on opportunities for continued growth

We are beginning 1988 with a very strong base of retail operations.

While we are pleased with the progress we have made, we are well aware that there is still much more to be done.

Our goal is to continue to be preeminent in the businesses we choose to enter and operate. We intend to be a major competitive force in each of our business segments.

We believe that efficient and low-cost operations are imperative to achieving our goals.

At Target we will continue to add new stores while increasing sales productivity in existing stores. We feel very positive about Target's past results and its new market performance, particularly its thrust into California. We are excited about Target's sales and profit potential in 1988 and beyond.

At Mervyn's we have slowed down square footage growth and will focus near-term on earnings growth.

In our department stores, we developed "Performance Plus," an innovative approach to selling and customer service. Also, we are focusing our fashion merchandise in the moderate to better price range and watching the balance closely.

At Lechmere we are carefully monitoring our recently expanded base of stores to determine how best to generate consistent earnings growth.

Overall, we are striving to be a leader in all facets of our business:

□ To serve our customers better than the competition.

□ To provide our employees with excellent opportunities for career growth.

□ To be a contributing corporate citizen, an integral part of all the communities where we do business.

By serving the interests of all these important constituencies, we will see to it that our shareholders receive the maximum return on their investment... now and in the future.

I can assure you that this past year has been both difficult and enlightening for all of us. The challenges we encountered included...

□ A lengthy takeover attempt of Dayton Hudson which was costly, not only in terms of expense, but also in management time and concern among our employees, customers, and suppliers.

□ A repositioning and, finally, the beginning of a turnaround at Mervyn's.

□ The stock market crash and its attendant erosion of consumer confidence just as the Christmas selling season was getting underway.

□ The successful opening of 73 Target stores, including 50 locations on the West Coast that were acquired in a major 1986 real estate transaction.

We not only met these challenges, but we learned from each experience.

We have emerged from 1987 as a stronger company, with a renewed incentive to perform and succeed! We are committed to achieving our objective of being the best at what we do. We will strive to be a premier growth corporation... anything less is not acceptable.

Sincerely,

Kenneth A. Macke
Chairman of the Board and
Chief Executive Officer

April 4, 1988

Merchandising

□ A major priority in 1987 was ensuring high quality in the merchandise we offer.

□ Our companies undertook steps to improve their fashion offering, strengthening their trend merchandising and sales promotion strategies.

□ To provide greater value to our customers, we began an aggressive program to lower everyday prices by passing on the benefits we receive from a lower income tax rate.

Customer Service

□ Keeping our stores fully stocked with the merchandise our customers want most continued to be a major priority in 1987.

□ We focused on keeping our stores up-to-date and convenient. Our companies introduced new store prototype designs and remodeled existing stores.

□ We introduced innovative programs which raise standards for customer service.

Technology

□ We installed new technological systems, including electronic bar-code scanning and automatic price look-up.

□ Technology aimed at improving efficiency and productivity included electronic communication with suppliers and new computerized distribution systems.

Home Furnishings Test Strategy

□ We continued to monitor the profit formula and merchandise mix of Branden's, our six-store home furnishings test strategy. During 1988, we will add three stores in existing Georgia and Florida markets to test efficiencies in advertising and distribution.

Dayton Hudson Corporation Operating Committee
Seated left to right:
Stephen E. Watson, *Chairman and CEO, Dayton Hudson Department Store Company;*
Bruce G. Allbright, *President, Dayton Hudson Corporation;*
Kenneth A. Macke, *Chairman and CEO, Dayton Hudson Corporation;*
Robert J. Ulrich, *Chairman and CEO, Target;*
James T. Hale, *Senior Vice President and General Counsel, Dayton Hudson Corporation.*
Standing left to right:
C. George Scala, *Chairman, President and CEO, Lechmere;*
Walter T. Rossi, *President and CEO, Mervyn's;*
Willard C. Shull, III, *Senior Vice President and Chief Financial Officer, Dayton Hudson Corporation.*

Corporate Operating Committee

□ We established a corporate operating committee to create a stronger partnership between corporate management and the management of our operating companies, and to bring corporate management closer to the customer.

□ The operating committee has a threefold mission: to conduct organized discussions of strategic, operating, and policy issues; to serve operational and developmental needs; and to improve communications.

Target

Target experienced the most dramatic growth in its history in 1987. The company added a record number of new stores, including 50 units primarily in California which were acquired in a major real estate transaction in 1986. Despite the expenses related to remodeling and opening these stores, Target once again reported record results, making 1987 its 13th consecutive year of increased earnings.

Robert J. Ulrich, Chairman and CEO, in the domestics and home decor department in a new Target store. The home area achieved strong results in 1987 after fashion and quality were upgraded.

1987 Highlights

□ Target opened 73 new stores, including units in five new markets: Detroit, Las Vegas, Reno, the San Francisco Bay area, and the San Joaquin Valley of California. The expansion increased retail space by 30%.

□ Total revenues increased 22% over the prior year. Sales from new stores were very strong. Comparable-store revenues rose 4%.

□ Operating profit increased 4% despite major store conversion expenses. Without these expenses, Target's operating profit would have been up 17%.

The Year in Review

Target continued to refine its merchandising strategies in 1987. Assortments in categories such as electronics, domestics, shoes, accessories, and children's were narrowed and updated to place more emphasis on key items. The home decor and domestics areas in particular achieved outstanding results after fashion and quality were upgraded.

Target continued to work toward lower everyday prices in 1987, with an aggressive effort to pass on to customers the benefits the company is realizing through a lower income tax rate. The company also introduced its "You'll Never Pay Less" program which guarantees customers that if they find a lower advertised price on any item at another store within 30 days, Target will refund the difference.

To speed the check-out process, Target installed electronic bar-code scanners in more than 100 stores in 1987. In addition to saving the customer's time, this technological enhancement provides for more accurate inventory data, which improves Target's ability to keep its shelves stocked with the merchandise customers want most.

Target began testing a new integrated store distribution system called Merchandise Flow. The test is aimed at improving both in-stock positions and profitability. Under the new system, Target's distribution centers deliver replenishment shipments to stores daily in quantities designed to fit on the selling floor. The project is being tested in one merchandise division in the Pueblo, Colorado distribution center, which serves 44 stores.

During 1987, Target developed and implemented an innovative store personnel program designed to give employees greater job satisfaction through more

hours for part-time workers, skill-based pay increases and additional benefits. The program, called Team Flex Staffing, is resulting in greater overall customer service by giving Target the flexibility to quickly increase staff in areas of the store where it is needed most.

Looking Ahead to 1988

□ A 25-store expansion program will include multi-store entries into three new states: Washington, Oregon and New Mexico. Additional stores also are planned for Michigan and California. New distribution centers with larger capacity to support planned growth will open in Sacramento and Indianapolis.

□ Electronic bar-code scanning will be installed throughout the entire chain by the end of the year.

□ The Merchandise Flow system will be expanded to two additional merchandise divisions. Inventory systems also will be enhanced to improve in-stock position.

(Millions of Dollars)	1987	1986	1985
Revenues	**$5,306.1**	$4,354.9	$3,931.5
Operating Profit*	**$ 322.5**	$ 311.0	$ 277.8
Stores	**317**	246	226
Retail Square Feet (000)**	**31,618**	24,260	22,414

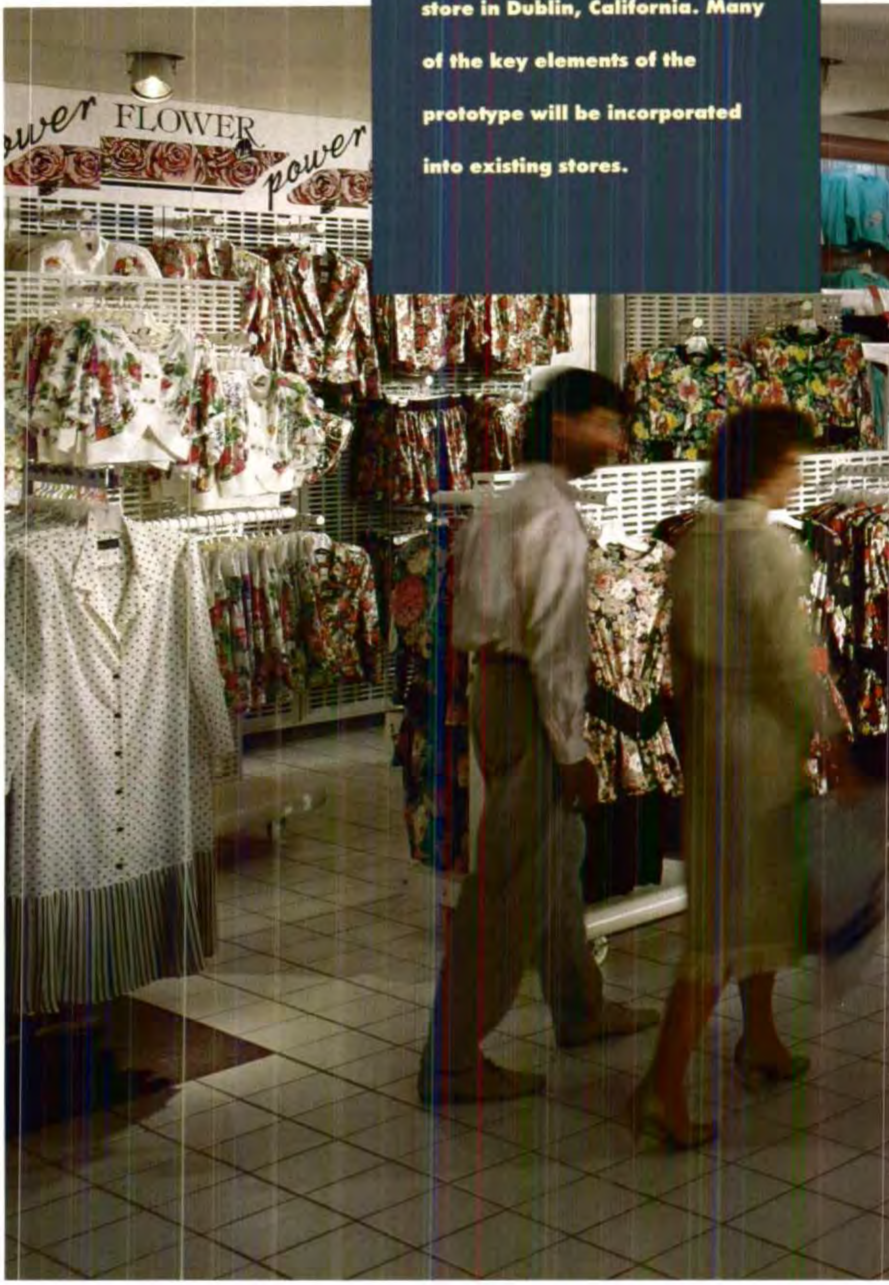
*Operating profit is LIFO earnings from operations before corporate expense, interest and income taxes.

**Total square feet less office, warehouse and vacant space.

Mervyn's

Mervyn's concentrated on the implementation of its three primary business strategies in 1987. The three strategies–merchandise direction, customer satisfaction, and expense management–are aimed at placing Mervyn's in a strong position between upscale discounters and department stores. Mervyn's also recorded the most successful new market entry in its history with a multi-store expansion in Michigan.

Walter T. Rossi, President and CEO, in Mervyn's new prototype store in Dublin, California. Many of the key elements of the prototype will be incorporated into existing stores.



1987 Highlights

- Total revenues increased 11% over the previous year. Revenues from comparable stores were up 1%.
- Operating profit declined 6% for the year. For the fourth quarter, operating profit rose substantially.
- Twenty four new stores opened, bringing the year-end total to 199. The openings included eight stores in Michigan markets and four stores in the Los Angeles area, increasing the total there to 36.
- Mervyn's achieved the lowest expense rate in its history.

The Year in Review

Significant steps were taken in 1987 in each of Mervyn's three principal business strategies to enhance the company's potential for continued growth.

Recognizing that quality is the most important element in the company's merchandise direction, Mervyn's created a product development organization to monitor and improve the quality of the merchandise offering. During 1987, a large number of key private-label items, including men's dress shirts, socks, and towels, were upgraded in quality.

Consistent with Mervyn's objective to improve its fashion trend execution, the company created a trend organization to monitor and introduce fashion trends on a more timely basis. Mervyn's sales promotion strategy also was upgraded to communicate to customers its new focus on fashion.

The most significant step taken in 1987 to improve customer service was the implementation of electronic bar-code scanning. The system was installed throughout the entire chain in just six months, making Mervyn's the first national softgoods retailer with electronic scanning.

Another technological customer service enhancement introduced in 1987 was a magnetic stripe reading system which automatically reads the information on credit cards.

The introduction of a new store prototype in 1987 is aimed at making shopping more pleasant and convenient for Mervyn's customers. In the new prototype, merchandise is grouped together to create the effect of several specialty stores or "worlds" such as Men's World and Home World. Ten "strike points" act as stages for dominant trend merchandise presentations. The prototype also

features new graphics, signing, and accent lighting.

Looking Ahead to 1988

□ In the area of merchandising, Mervyn's will concentrate on the strategies begun in 1987: a refinement of assortments, more competitive pricing, better in-stock positions, sharper trend execution, improved quality, and upgraded sales promotion.

□ Customer service programs will be supported by the implementation of many of the key elements of the new store prototype into the existing stores. A broader store remodel prototype also will be developed for use in the future.

□ Expense management will continue to be a major focus. Mervyn's expects technological improvements like electronic communication with suppliers to begin to produce expense savings in 1988.

□ Mervyn's will open 15 stores in 1988. The new units will be primarily additions to existing markets.

(Millions of Dollars)	**1987**	1986	1985
Revenues	**$3,182.6**	$2,862.3	$2,527.0
Operating Profit	**$ 150.4**	$ 160.2	$ 245.0
Stores	**199**	175	148
Retail Square Feet (000)	**15,727**	13,839	11,733

Dayton Hudson Department Store Company (DHDSC) continued to work toward expanding its share of the moderate and better fashion business in 1987. Major steps taken during the year included an upgrading of merchandise fashion and quality, continued expansion of a major new customer service program, and ongoing improvements in store design and merchandise presentation.

1987 Highlights

- Revenues declined 1% from the previous year, reflecting the elimination of several merchandise departments as well as an industry-wide slowdown in apparel sales.
- Operating profit fell 26% due to lower sales and a decline in the gross margin rate.
- Major store remodeling projects in three Dayton's stores and 10 Hudson's stores were the most the company has undertaken in a single year.

The Year in Review

DHDSC continued to refine and refocus its merchandising strategy in 1987, eliminating several merchandise areas that were inconsistent with the company's direction.

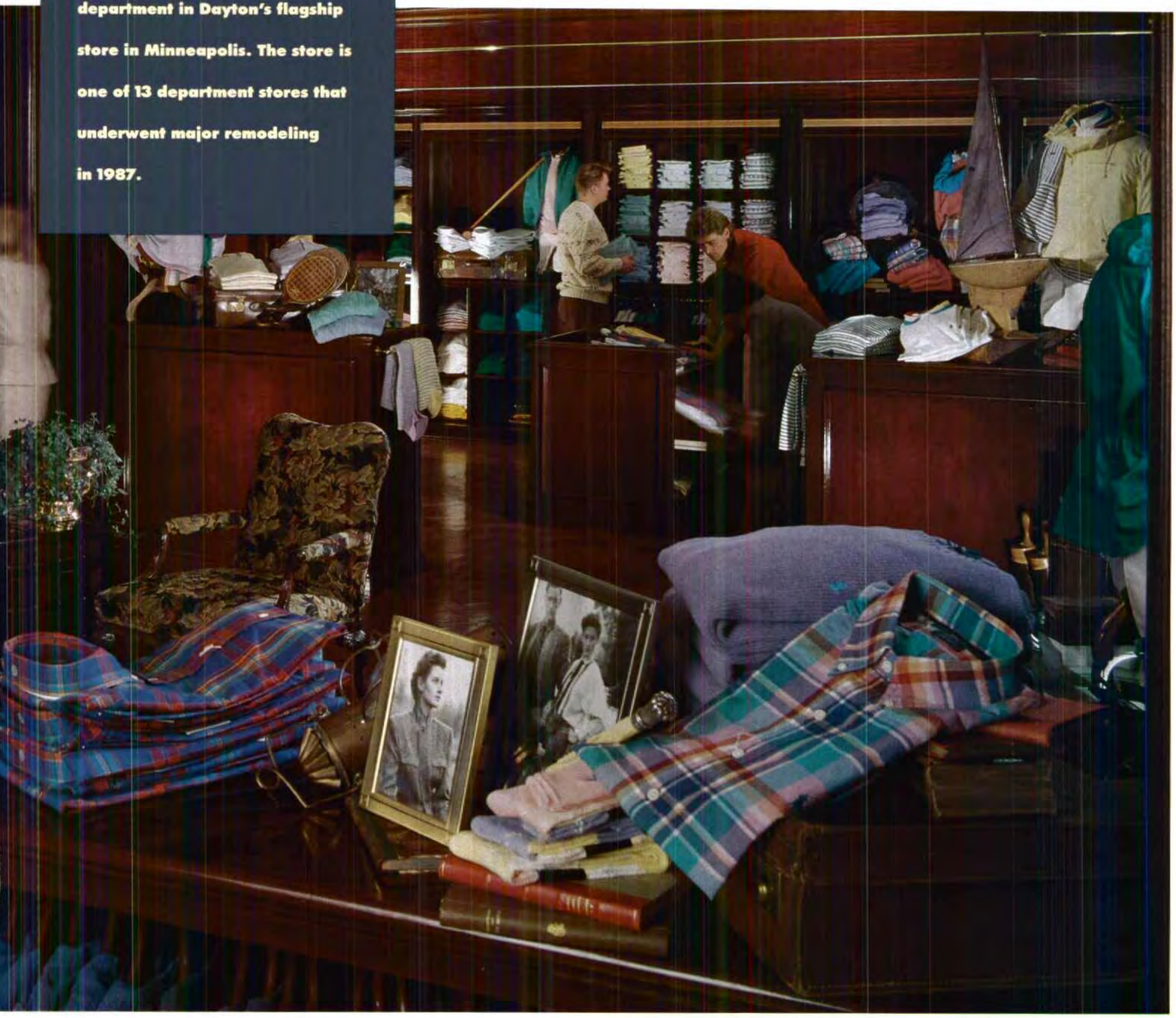
Other merchandising changes included a realignment of women's apparel by lifestyle to reduce the number of areas with similar items and make shopping more convenient for the customer.

The furniture and carpet departments in Hudson's stores were consolidated into fewer, larger furniture floors, with a net increase in furniture sales. The consolidation also resulted in an increase in space for apparel.

Performance Plus, a major program aimed at improving customer service, was rolled out to ready-to-wear areas in 21 stores and throughout the entire Hudson's store in Grand Rapids, Michigan. The program raises standards for customer service and provides employees with potential for increased pay and greater opportunities for career advancement. Test results indicate that the program will be successful in enhancing customer service and producing incremental sales.

Advances in technology helped to improve service and reduce costs in 1987. The company intensified its commitment to the utilization of UPC codes, testing full price look-up, electronic wanding in selected departments, and electronic data interchange with an increasing number of suppliers. All credit functions were consolidated during the year, resulting in increased productivity and lower expenses.

Stephen E. Watson, Chairman and CEO, in the Ralph Lauren Polo department in Dayton's flagship store in Minneapolis. The store is one of 13 department stores that underwent major remodeling in 1987.



Looking Ahead to 1988

□ DHDSC will continue to remodel stores so that they remain fresh, up-to-date, and convenient for the customer. Major remodeling programs are scheduled for seven Hudson's stores and five Dayton's stores in 1988.

□ The Performance Plus customer service program will be expanded to two additional full stores as well as additional departments. A modified program for small markets will be tested in the Fargo, North Dakota store.

□ Career apparel for both men and women is expected to be a major growth category for DHDSC in 1988. The home area, particularly domestics and furniture, is expected to do well. DHDSC will focus on key fashion resources in the moderate price range in 1988.

(Millions of Dollars)	**1987**	1986	1985
Revenues	**$1,552.3**	$1,566.3	$1,447.9
Operating Profit	**$ 122.4**	$ 165.8	$ 121.8
Stores	**37**	37	37
Retail Square Feet (000)	**7,791**	7,791	7,904

For Lechmere, 1987 was a year of continued rapid growth. With the expansion completed during the year, the company has grown from 10 stores to 24 stores in just two years. Lechmere also introduced a new store prototype in 1987, and continued to refine its offering of high-quality, value-priced electronics products, appliances, housewares, and leisure-time equipment.

1987 Highlights

□ Seven stores opened, four in Northeastern markets and three in new markets in the Southeast: Raleigh, North Carolina; Clearwater, Florida; and Sarasota, Florida.

□ Total revenues increased 34%. Revenues from comparable stores rose 6%. New stores opened during the year reported very strong sales.

□ Operating profit increased 16% despite significant expenses related to expansion.

The Year in Review

Refinements in Lechmere's merchandising strategy focused on the expansion of several targeted growth categories, including home office equipment, ready-to-assemble furniture, ceiling fans, housewares and storage items, athletic shoes, and sporting goods.

Lechmere also entered the rapidly growing home health care market with a four-store test featuring quality, brand-name merchandise for use in the home. Products tested were selected from seven categories: stress management, health measurement, mobility and bathing aids, professional health treatment, environmental measurement and treatment, oral hygiene, and scales.

Other merchandising programs implemented during the year included a company-wide focus on accessory products.

Among the seven new units opened in 1987 was a new prototype store in Sarasota, Florida. The 60,000-square-foot store, which compares with the standard 80,000-square-foot unit, features new interior and exterior signing, a new color scheme, and an exposed ceiling to give the store the look and feel of an open warehouse. Indications are that the sales potential may be as great in the smaller store as in the traditional 80,000-square-foot store.

Lechmere incorporated a number of technological improvements in 1987. New checkout terminals designed to improve accuracy and reduce transaction time were installed in all stores. A computerized price look-up system was introduced. New logistics systems lowered distribution expense significantly and improved in-stock positions.

Customer service programs introduced during the year included a more liberal return policy and a price-guarantee program, which assures customers that Lechmere will match the market's lowest prices on any item.

During 1987, Lechmere reorganized its

C. George Scala, Chairman, President and CEO, in Lechmere's home office department in the Nashua, New Hampshire store. Lechmere expects continued strong growth in the home office category in 1988.

commission selling management program to upgrade sales positions, establish new performance standards, and provide more opportunity for career growth.

Looking Ahead to 1988

□ Lechmere will slow its expansion in 1988 to focus on improving productivity and profitability. Three 60,000-square-foot stores are scheduled to open during the year, each in a new market: Salem, New Hampshire; Greenville, South Carolina; and Charlotte, North Carolina.

□ Sales of home office products are expected to continue to grow as more people work out of their homes and small business formations increase. New product introductions also should fuel rising sales in this rapidly growing area.

□ The market for home health care merchandise looks equally promising. In 1988, Lechmere will introduce home health care products in all stores to take advantage of the expected growth.

(Millions of Dollars)	**1987**	1986	1985
Revenues	**\$636.3**	\$475.6	\$348.9
Operating Profit	**\$ 22.7**	\$ 19.5	\$ 19.8
Stores	**24**	17	10
Retail Square Feet (000)	**2,317**	1,782	1,154

Dayton Hudson Corporation Board of Directors
Seated left to right:
Betty Ruth Hollander, *The Omega Group, Inc.*;
Livio D. DeSimone, *3M Company*;
Robert A. Burnett, *Meredith Corporation*;
Bruce K. MacLaury, *The Brookings Institution*;
Kenneth A. Macke, *Dayton Hudson Corporation*;
Roger L. Hale, *Tennant Company*;
Bruce G. Allbright, *Dayton Hudson Corporation.*
Standing left to right:
David T. Kearns, *Xerox Corporation*;
David T. McLaughlin, *The Aspen Institute for Humanistic Services*;
Rand V. Araskog, *ITT Corporation*;
John A. Rollwagen, *Cray Research, Inc.*;
Donald J. Hall, *Hallmark Cards, Incorporated.*

At Dayton Hudson, we consider effective corporate governance to be the very foundation of successful corporate management. Accordingly, our Board of Directors plays a key role in our success as a Corporation.

The mission statement of our Board describes its role as follows: "As representatives of the shareholders, to be the primary force pressing the Corporation to the realization of its opportunities and the fulfillment of its obligations to its shareholders, customers, employees and the communities in which it operates."

We believe that the ability of the Board to achieve this mission is directly related to the quality of its members. We look for directors who have a proven record of accomplishment–individuals who are at the peak of their careers. We seek people who have experience, integrity and intelligence. We also seek a diversity in professional backgrounds and personal qualifications, so that our Board has the balance of perspectives that we believe is essential to the effective governance of our Corporation.

We recognize that an independent Board of Directors also is necessary for effective corporate governance. Our directors must have the freedom and independence to question, challenge and stimulate management. Our objective is to have a Board made up predominately of directors from outside the day-to-day management of the Corporation. At present, only two representatives from management serve on our 12-member Board.

In all our dealings between management and the Board of Directors, we strive for an open and dynamic relationship. We believe that such a relationship is the best assurance to our shareholders that the Corporation's future is secure.

1987 Highlights

□ Capital investment, including the present value of new operating leases, totaled $876 million. That compares with an investment of $1.09 billion in 1986.

□ The gross margin rate declined, reflecting a highly competitive retail environment and a commitment by our companies to pass on to the customer the savings resulting from a lower income tax rate.

□ The operating expense rate improved, continuing the trend in each of the last six years.

□ Interest expense rose due to increased levels of debt offset in part by savings resulting from the purchase and redemption of high-interest rate debt in 1986.

□ Our income tax rate was 42.9%, down from 48.4% a year ago.

□ Dividends declared totaled $.94½ per share, an increase of 10% over $.86 per share a year ago.

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(Millions of Dollars, Except Per Share Data)

Our objective is to provide shareholders with a superior return on their investment through a combination of stock price appreciation and current income, while maintaining a flexible and conservative capital structure.

Performance Objectives

- Return on equity of 18%.
- Annual EPS growth of 15%.

Achievement of our financial performance objectives depends largely upon our ability to produce a superior return on investment (ROI). ROI is the most important single measure of financial performance and it is the primary financial tool we use to manage our business. We define ROI as the after-tax return on investment before borrowing costs.

ROI is an important part of the following management processes:

- *Performance Appraisal.* The incentive compensation of management is based on return on investment, as well as on growth in earnings.
- *Capital Allocation.* We allocate capital for expansion of each operating company based on the actual and projected performance measured against its ROI standard. Additional criteria for allocating capital include the quality of the company's strategic plan, strength of the management team, its systems and development of market position.
- *Capital Project Evaluation.* All capital projects are expected to achieve ROI levels which will produce an internal rate of return over their life of 13%. We audit actual results in the years following completion to determine actual individual project performance.

Return on Investment	**1987**	1986	1985
Net earnings from continuing operations	**$ 228.4**	$ 255.0	$ 280.5
Interest expense–after tax (a)	**74.5**	55.9	49.9
Interest equivalent in operating leases–after tax (b)	**26.4**	16.8	14.7
Earnings before financing costs	**$ 329.3**	$ 327.7	$ 345.1
Working capital (c)	**$1,203.5**	$1,104.3	$ 943.4
Net property and equipment	**2,402.3**	1,655.7	1,418.6
Other non-current assets	**147.4**	22.3	13.0
Capital leases	**114.9**	114.7	114.7
Present value of operating leases	**382.2**	258.1	230.0
Total investment at beginning of year	**$4,250.3**	$3,155.1	$2,719.7
Return on investment	**7.7%**	10.4%	12.7%

(a) Interest expense on beginning-of-year debt and capital leases.
(b) Assumes after-tax interest cost of approximately 7% on beginning-of-year present value of operating leases for 1987, and 6½% for 1986 and 1985.
(c) Current assets less non-interest bearing current liabilities.

Financial Policies

- Maintain strong investment grade ratings on our debt. Our long-term debt and commercial paper carry very strong ratings from the major rating agencies.
- A target debt ratio of 45% of total capitalization, including capital leases and the present value of operating leases. Our 1987 debt ratio exceeded our target due to the share repurchase program. We believe this action will produce an excellent value for our shareholders.

Key Financial Ratios

Continuing Operations			**1987**	1986	1985	Description of Ratios:
Return on Sales	=	Earnings / Sales	**3.1%**	3.6%	4.2%	Return on sales indicates the amount of profit per dollar of sales before financing costs.
times						
Investment Turnover	=	Sales / Investment	**2.5x**	2.9x	3.0x	Investment turnover provides a measure of the sales generated from each dollar invested in our business.
equals						
Return on Investment	=	Earnings / Investment	**7.7%**	10.4%	12.7%	Return on investment provides a measure of profit generated from each dollar invested before financing costs.
Return on Equity	=	Net Earnings / Equity	**10.5%**	13.1%	16.2%	Return on equity provides a measure of profit generated per dollar of shareholder investment.

Investment and equity are beginning of period.

(Millions of Dollars, Except Per-Share Data)

Capitalization	1987	1986	1985
Notes Payable	$ 353.3	$ —	$ —
Long-term debt (a)	1,697.4	1,250.5	814.2
Capital leases (a)	139.7	136.7	133.2
Present value of operating leases	376.1	382.2	258.1
Total debt and equivalent	2,566.5	1,769.4	1,205.5
Deferred items	285.0	301.4	121.4
Equity	1,986.0	2,179.5	1,947.4
Total capitalization	$4,837.5	$4,250.3	$3,274.3
Debt ratio (total debt and equivalent as a percentage of total capitalization)	53%	42%	37%

(a) Including current portion.

The majority of our growth will continue to be financed with internally generated funds. The remainder will be financed with a mix of debt which is consistent with the cash flow characteristics of our capital investments.

Because of the lead times required for planning and construction of our stores, we make commitments before actual capital expenditures occur. Our financial policies limit the amount of these forward commitments to a level which could be funded by projected internally generated funds.

Capital Investment

Target and Mervyn's continue to receive the majority of our capital investment, which totaled $876 million in 1987. Capital investment in 1988 is expected to exceed $600 million.

Capital Investment	1987	1986	1985
Capital expenditures	$839	$ 941	$403
Present value of new operating leases	37	148	41
Total	$876	$1,089	$444

Dividends and Common Stock Price Per Share

In support of our goal of providing our shareholders with a superior return on their investment, it is our policy to make regular annual increases in dividends on common stock.

Dividends declared in 1987 totaled $.94½ per share, a 10% increase over the $.86 per share declared in 1986.

The quarterly dividend was increased to $.25½ per share paid in the first quarter of 1988. The current annualized rate is $1.02 per share.

Dayton Hudson Corporation common stock is listed on the New York Stock Exchange and the Pacific Stock Exchange with the symbol DH, and abbreviated in newspaper listings as DaytHd.

At year-end, the number of Dayton Hudson shareholders of record was 16,684, compared with 15,480 at year-end 1986. On April 4, 1988, there were 16,220 shareholders of record and the common stock price was $37½.

	Quarterly Dividend Declared per Share		Common Stock Price Range			
			1987		1986	
Fiscal Quarter	1987	1986	High	Low	High	Low
First	$.23	$.21	$48½	$38¾	$55⅞	$40⅜
Second	.23	.21	63	41¾	58½	44¼
Third	.23	.21	60½	21½	48⅛	40
Fourth	.25½	.23	35	25⅛	47¾	40¾
Total Year	$.94½	$.86	$63	$21½	$58½	$40

Revenues increased 15% in 1987 largely due to our expansion. Comparable-store revenues (revenues from stores open longer than 12 months) rose 2%. Our results follow a total revenue increase of 12% and a comparable-store revenue increase of 5% in 1986. Net earnings from continuing operations declined 10% in 1987. The decline is primarily the result of a reduction in gross margin rate as well as increased start-up and interest expense. In 1986, our earnings declined 9% and in 1985, earnings increased 14%.

The following table illustrates the impact of the major factors contributing to the changes in our earnings per share from continuing operations since 1985.

Variance analysis:	1987 vs. 1986	1986 vs. 1985
Prior year's earnings per share	$2.62	$2.89
Change in earnings per share due to:		
Revenues	.44	.39
Gross margin rate	(.71)	(.71)
Operating expense rate	.30	.33
Start-up expenses	(.24)	(.06)
Interest expense, net	(.15)	(.10)
Income tax rate	.23	(.13)
Corporate expense and other factors, net	(.11)	.01
Stock repurchase, net *	.03	—
Earnings per share	$2.41	$2.62

*Stock repurchase includes the positive impact of a reduced number of average shares outstanding partially offset by the interest on additional debt to finance the buyback.

Revenues

The major portion of our revenue growth continues to be generated by Target and Mervyn's, primarily due to their aggressive expansion over the last few years. DHDSC reported a slight decline in revenues, while Lechmere showed a significant revenue increase resulting from expansion as well as base business growth.

Revenue Increases/ (Decreases)	1987		1986		1985	
	All Stores	Comparable Stores	All Stores	Comparable Stores	All Stores	Comparable Stores
Target	22%	4%	11%	5%	11%	6%
Mervyn's	11	1	13	4	18	8
DHDSC	(1)	(1)	8	8	4	4
Lechmere	34	6	36	4	25	8
Total	15%	2%	12%	5%	12%*	6%

*Comparison excludes revenues from Diamond's and John A. Brown which were sold in 1984.

One measure we use to evaluate the productivity of our stores is revenues per square foot.

Revenues Per Square Foot* (Unaudited) (Dollars)	1987	1986	1985
Target	$193	$188	$180
Mervyn's	$216	$226	$233
DHDSC	$199	$201	$184
Lechmere	$323	$328	$340

*Thirteen-month average retail square feet.

Productivity is typically lower in new stores and improves as stores mature. Target, however, showed improvement in revenues per square foot in 1987 despite 73 new store openings.

Included in our revenues is finance charge revenue of $143.4 million on internal credit sales of $2.40 billion in 1987, $151.4 million on sales of $2.39 billion in 1986, and $144.1 million on sales of $2.27 billion in 1985.

Gross Margin Rate and Inventories

Our overall gross margin rate (excluding buying and occupancy) declined in 1987, reflecting a highly competitive retail environment and our commitment to pass on to the consumer the income tax rate reduction of the Tax Reform Act of 1986. The relative growth of Target and Lechmere, our low-margin companies, also contributed to the decline in our overall gross margin rate. This is in keeping with our strategy to build sales volume with a focus on generating strong increases in gross margin dollars. Substantial declines in the gross margin rates of Mervyn's and DHDSC are due in part to higher promotional markdowns. Mervyn's rate is also impacted by the ongoing strategy of providing better value to customers. Target and Lechmere reported slightly lower gross margin rates.

The 1986 overall gross margin rate was lower than 1985 due to a significant reduction at Mervyn's. DHDSC's gross margin rate improved significantly in 1986, while the rates at Target and Lechmere declined slightly.

We use the last-in, first-out (LIFO) method of valuing inventories and determining cost of sales. The LIFO provision included in cost of retail sales was a charge of $21.5 million ($.13 per share) in 1987, compared with a charge of $37.9 million ($.20 per share) in 1986, and a charge of $13.5 million ($.08 per share) in 1985. The decrease in the 1987 provision was due primarily to inventory growth necessitated by our rapid expansion. The increase in the 1986 provision was due to lower markups.

The cumulative LIFO provision was $110.4 million at January 30, 1988 and $179.5 million at January 31, 1987. The lower balance at January 30, 1988, reflects a reduction of FIFO inventories and the cumulative LIFO provision by equal amounts. There is no impact on the LIFO inventory balance.

Operating Expense Rate

Our 1987 operating expense rate improved compared with 1986, continuing a trend of improvement in each of the last six years. This stems from our continued emphasis on operating expense control. Additionally, the lower operating expense rates of Target and Lechmere favorably impacted the consolidated rate due to these companies' relative growth. Target, Mervyn's and Lechmere improved their operating expense rates in 1987, while DHDSC's rate increased primarily due to lower sales and the higher payroll costs associated with an improved customer service program. Operating expenses include buying and occupancy costs, selling, publicity and administrative expenses, depreciation, rent and taxes other than income taxes.

Start-up Expenses

Increased start-up expenses in 1987 reflect Target's major expansion on the West Coast. The start-up, rent and other costs incurred in 1987 relating to the conversion of 50 store sites acquired in late 1986 amounted to $42.9 million ($.26 per share).

Interest Expense

Our interest costs have risen primarily due to increased levels of debt offset in part by savings resulting from the purchase and redemption of high-interest rate debt in 1986. The additional debt in 1987 was used for capital expansion and store remodeling, to finance the stock repurchase program, and to fund inventory levels necessary to stock new stores.

Interest expense includes interest costs incurred on debt and capital leases. This expense is reduced by the amount of interest capitalized as part of an asset's cost during a period of construction or remodeling. Interest expense also is reported net of interest income, which results from the temporary investment of seasonal cash flows and proceeds from debt issues.

Components of Interest Expense, Net	1987	1986	1985
Interest on debt	**$146.3**	$127.7	$ 95.4
Interest on capital leases	**16.6**	16.4	16.5
Interest cost capitalized	**(6.7)**	(6.7)	(4.7)
Interest income	**(4.4)**	(19.9)	(7.4)
Net expense	**$151.8**	$117.5	$ 99.8

Income Taxes

Our effective income tax rate was 42.9% in 1987, 48.4% in 1986 and 45.8% in 1985. The benefit of a lower tax rate in 1987 resulting from the Tax Reform Act is partially offset by the loss of investment tax credits. The increase in the 1986 rate was primarily the result of the loss of investment tax credits. Our effective tax rates for 1987, 1986 and 1985 vary from the federal statutory rate as follows:

Percent of Earnings Before Income Taxes	1987	1986	1985
Statutory rate	**39.0%**	46.0%	46.0%
State income taxes, net of federal tax benefit	**4.1**	3.9	3.9
Tax credits, net*	**(.6)**	(2.0)	(3.6)
Other	**.4**	.5	(.5)
Effective tax rate	**42.9%**	48.4%	45.8%

*Net tax credits, primarily investment tax credits and targeted jobs tax credits, were $2.3 million in 1987, $9.9 million in 1986 and $18.4 million in 1985.

We anticipate that our effective income tax rate will be approximately 40% in 1988.

The components of our provision for income taxes for the past three years are as follows:

	1987	1986	1985
Current: Federal	**$169.7**	$170.7	$160.8
State	**32.2**	30.2	30.2
	201.9	200.9	191.0
Deferred: Federal	**(25.3)**	33.2	39.2
State	**(5.2)**	5.1	7.1
	(30.5)	38.3	46.3
Total	**$171.4**	$239.2	$237.3

We provide deferred income taxes for income and expenses which are recognized in different years for financial and tax reporting. Our deferred tax provision is comprised of the following timing differences:

	1987	1986	1985
Depreciation expense	**$ 40.4**	$36.6	$32.3
Installment sales deferred income	**(38.3)**	(1.1)	14.3
Inventory cost capitalization	**(11.1)**	—	—
Bad debt expense	**(1.9)**	—	—
Vacation pay expense	**(6.2)**	—	—
Other	**(13.4)**	2.8	(.3)
Provision for deferred taxes	**$(30.5)**	$38.3	$46.3

The Tax Reform Act of 1986 repealed installment sale reporting of income from revolving credit plans effective for 1987 and thereafter. The 1986 year-end deferred income from installment sales must be included in taxable income during a four-year transition period.

The Tax Reform Act also included tax changes which have created new timing differences in 1987. The 1987 beginning-of-year inventory for tax purposes was recomputed using new capitalization rules. The 1987 beginning-of-year allowance for doubtful accounts and the additional inventory resulting from the new capitalization rules must be included in taxable income during the four-year transition period. In addition, the vacation pay accrual deduction was limited to amounts paid within eight and one-half months of year-end.

In December 1987, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes." Companies are required to adopt the new method of accounting for income taxes no later than 1989. The impact of the change in accounting method may be shown as an accounting change adjustment to income in the year of adoption or prior-year financial statements may be restated to reflect the new rules. The Statement requires a liability method of accounting for income taxes. We plan to adopt the Statement at the beginning of our 1989 fiscal year. If we restate 1987 financial statements to comply with the requirements of the Statement, we estimate that 1987 beginning-of-year retained earnings would increase and deferred tax liabilities would decrease by approximately $55 million.

Corporate Expense and Other Items

Corporate expense and other items for the past three years are as follows:

	1987	1986	1985
Corporate headquarters expense	**$18.4**	$17.4	$17.8
Other	**48.0**	36.8	39.4
Total	**$66.4**	$54.2	$57.2

The major components of other are the net results of operations of our test strategies and charitable contributions in support of our 5% giving program. In 1987, other also includes one-time expenses of $9.1 million related to an unsolicited takeover proposal, a loss of $5.0 million resulting from ending our telemarketing test strategy, and $4.6 million related to the restructuring and consolidation of our corporate headquarters. These one-time expenses were partially offset by income of $5.0 million related to the sale of B. Dalton Bookseller.

Effect of Inflation

Inflation during the past three years has been minimal. As a result, reported revenue increases closely represent real growth rather than growth through increasing prices. We use the LIFO inventory accounting method for reporting purposes. We believe LIFO provides a better matching of current costs with revenues than does the first-in, first-out (FIFO) method. Consequently, the cost of goods sold included in our results of operations are already reported in real terms.

While the rate of inflation has eased in recent years, property, equipment and capital leases include the cumulative effects of periods of both high and low inflation. If these assets had been acquired at current costs, our related depreciation and amortization would have been approximately 30% higher in each of the last three years.

Significant Events

- *Stock Repurchase.* On October 21, 1987, the Board of Directors authorized purchase by the Corporation of up to 15 million shares of its common stock from time to time. At January 30, 1988, we had purchased 11.8 million shares at an average price of approximately $29 per share.
- *Real Estate and Lease Acquisition.* In 1986, Target entered into an agreement covering 78 stores located primarily in California. Fifty of these stores were remodeled and opened in 1987 as Target stores. Twenty-two of the sites acquired but not scheduled for conversion were sold during 1987.
- *Discontinued Operations.* Effective December 27, 1986, we sold B. Dalton Bookseller. The gain on the sale (less income taxes of $31.3 million) was $85.2 million. B. Dalton discontinued its Pickwick Discount Books test strategy in 1986. Our consolidated financial statements and related information for fiscal 1986 and prior years reflect B. Dalton and Pickwick as discontinued operations.

Results of Discontinued Operations	**1986* 47 Weeks Ended December 27, 1986**	1985 52 Weeks Ended February 1, 1986
Revenues	**$514.7**	$538.1
Earnings before income taxes	**$ 3.6**	$ 6.7
Income taxes	**(1.5)**	(3.6)
Net earnings	**$ 2.1**	$ 3.1

*Results from Pickwick included through July 5, 1986.

- *Extraordinary Charge.* During 1986, we purchased and redeemed a significant portion of our high-interest rate debt at a premium above par. This purchase and redemption resulted in an extraordinary charge of $32.3 million (net of a tax benefit of $32.6 million). The replacement of the debt at lower interest rates is resulting in interest expense savings.

Business Segment Trends

As shown in the business segment comparisons on the next page, Target and Mervyn's continue to contribute the greatest portion of our revenues. These two companies contributed 88% of our increase in revenue dollars over the past five years. Lechmere's revenues have had the highest compound growth rate over that period at 28%.

Operating profit has increased at a compound growth rate of 8% over the last five years. Target's contribution to total operating profit has increased from 35% to 52% over the five-year period.

Total operating profit declined 6% in 1987. Target had an increase in operating profit in 1987 despite expenses related to the conversion of 50 store sites acquired in 1986. The decline in operating profit at Mervyn's reflects lower earnings throughout the first three quarters of the year, while DHDSC's substantial decline was due to a lower gross margin rate and a decline in sales. Lechmere achieved higher operating profit in 1987 despite major expenses related to the opening of seven new stores.

Business Segment Comparisons (Millions of Dollars)	1987	1986	1985	1984*	1983	1982
Revenues						
Target	**$ 5,306.1**	$4,354.9	$3,931.5	$3,550.1	$3,118.4	$2,412.4
Mervyn's	**3,182.6**	2,862.3	2,527.0	2,141.1	1,688.9	1,335.8
Department stores	**1,552.3**	1,566.3	1,447.9	1,547.8	1,483.9	1,350.2
Lechmere	**636.3**	475.6	348.9	280.2	227.0	188.0
Total	**$10,677.3**	$9,259.1	$8,255.3	$7,519.2	$6,518.2	$5,286.4
Operating profit						
Target	**$ 322.5**	$ 311.0	$ 277.8	$ 235.6	$ 176.8	$ 150.1
Mervyn's	**150.4**	160.2	245.0	223.3	184.5	152.3
Department stores	**122.4**	165.8	121.8	106.7	155.7	114.4
Lechmere	**22.7**	19.5	19.8	20.2	18.8	12.0
Total	**618.0**	656.5	664.4	585.8	535.8	428.8
Interest expense, net	**151.8**	117.5	99.8	97.7	86.1	64.9
Corporate and other	**66.4**	54.2	57.2	47.4	40.2	10.2
Corporate and interest expense absorbed by discontinued operations	**—**	(9.4)	(10.4)	(12.8)	(6.4)	(4.4)
Earnings from continuing operations before income taxes and extraordinary charge	**$ 399.8**	$ 494.2	$ 517.8	$ 453.5	$ 415.9	$ 358.1
Operating profit as a percent of revenues						
Target	**6.1%**	7.1%	7.1%	6.6%	5.7%	6.2%
Mervyn's	**4.7**	5.6	9.7	10.4	10.9	11.4
Department stores	**7.9**	10.6	8.4	6.9	10.5	8.5
Lechmere	**3.6**	4.1	5.7	7.2	8.3	6.4
Assets						
Target	**$ 2,638.3**	$2,178.6	$1,518.8	$1,374.9	$1,257.8	$1,056.2
Mervyn's	**2,113.6**	1,817.4	1,614.5	1,328.9	1,064.2	821.3
Department stores	**760.8**	738.6	737.9	727.2	863.3	819.5
Lechmere	**430.9**	317.5	209.9	151.0	105.4	89.2
Discontinued operations	**—**	—	221.4	204.0	185.7	152.6
Corporate and other	**131.9**	229.9	115.0	13.9	118.5	46.5
Total	**$ 6,075.5**	$5,282.0	$4,417.5	$3,799.9	$3,594.9	$2,985.3
Depreciation						
Target	**$ 103.7**	$ 76.3	$ 70.0	$ 65.7	$ 56.4	$ 42.1
Mervyn's	**81.7**	67.5	54.5	42.7	30.0	23.6
Department stores	**29.7**	28.0	27.3	31.9	33.0	31.2
Lechmere	**10.9**	7.8	4.5	3.1	2.0	1.8
Corporate and other	**4.9**	3.1	1.9	1.5	1.7	.7
	230.9	182.7	158.2	144.9	123.1	99.4
Less depreciation on capital leases	**8.0**	8.1	8.0	8.1	7.7	7.9
Total	**$ 222.9**	$ 174.6	$ 150.2	$ 136.8	$ 115.4	$ 91.5
Capital expenditures						
Target	**$ 500.7**	$ 598.0	$ 138.3	$ 109.8	$ 143.4	$ 137.5
Mervyn's	**207.6**	243.5	176.6	165.4	138.3	95.7
Department stores	**48.6**	30.5	36.8	33.5	26.5	27.8
Lechmere	**72.2**	48.6	42.1	24.5	5.7	2.9
Corporate and other	**9.7**	20.3	9.2	2.9	6.8	4.3
	838.8	940.9	403.0	336.1	320.7	268.2
Less expenditures on capital leases	**8.2**	9.1	7.9	10.5	25.6	11.9
Total	**$ 830.6**	$ 931.8	$ 395.1	$ 325.6	$ 295.1	$ 256.3

*Consisted of 53 weeks.

Department stores include Diamond's and John A. Brown through September 29, 1984.

Quarterly Results (Unaudited)

We achieved double-digit increases in total revenues during each quarter of 1987. Comparable-store revenues were equal to last year in the fourth quarter, and showed modest growth in the first three quarters of the year. Earnings in the fourth quarter increased 11% over the same period in 1986. Net earnings were below last year in the first three quarters of 1987 due to declines in gross margin rates and increased start-up expenses.

The table below summarizes our results by quarter for 1987 and 1986.

We follow the same accounting policies in preparing our quarterly financial data as we do in preparing our annual data, with the following modifications:

- We expense costs of opening new stores evenly throughout the year in which they are incurred.
- We recognize real estate taxes, bonuses, professional fees and benefit plan expenses throughout the year based on anticipated annual amounts.
- We incur additional rental expense on the majority of our leased stores if the stores' annual sales exceed certain stipulated amounts. We estimate and record this additional rent each month based on actual monthly sales.
- We use our anticipated effective annual tax rate to compute income taxes on our quarterly earnings.
- During the year, we forecast our annual LIFO expense based on estimates of three factors: inflation rates (based on the Department Stores Inventory Price Index published by the Bureau of Labor Statistics), inventory levels and markup levels. We adjust our forecast quarterly and allocate the revised projected expense based on our historical experience of quarterly sales. In the fourth quarter of each year, we record the final adjustment reflecting the difference between our prior quarter estimate and actual LIFO expense. The following table shows the LIFO impact on earnings per share as reported and as reallocated if we had known the final inflation rates, inventory levels and markup rates when we made our quarterly accruals.

LIFO Expense/(Credit)	As Reported			Reallocated		
Quarter	**1987***	1986	1985	**1987***	1986	1985
First	**$ .05**	$ .04	$ .05	**$ .02**	$ .04	$ .01
Second	**.06**	.03	.03	**.03**	.04	.02
Third	**.02**	.09	.04	**.03**	.05	.02
Fourth	**(.01)**	.04	(.04)	**.05**	.07	.03
Total Year	**$ .13**	$ .20	$ .08	**$ .13**	$ .20	$ .08

*LIFO expense per share is computed based on average shares outstanding during the period. In 1987, the sum of the quarterly LIFO expense per share may not equal the total year amount because of the impact of the stock repurchase program on average shares outstanding.

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter		Total Year	
	1987	1986	**1987**	1986	**1987**	1986	**1987**	1986	**1987**	1986
Revenues	**$2,153.1**	$1,886.7	**$2,306.2**	$2,041.7	**$2,538.9**	$2,215.2	**$3,679.1**	$3,115.5	**$10,677.3**	$9,259.1
Gross profit*	**$ 606.3**	$ 547.2	**$ 596.8**	$ 559.8	**$ 674.0**	$ 617.1	**$ 947.6**	$ 829.8	**$ 2,824.7**	$2,553.9
Net Earnings:										
Continuing	**$ 38.1**	$ 40.5	**$ 23.0**	$ 40.6	**$ 33.6**	$ 53.1	**$ 133.7**	$ 120.8	**$ 228.4**	$ 255.0
Discontinued	**—**	(1.9)	**—**	(3.9)	**—**	(1.1)	**—**	9.0	**—**	2.1
Gain on Sale of B. Dalton	**—**	—	**—**	—	**—**	—	**—**	85.2	**—**	85.2
Extraordinary Charge	**—**	—	**—**	—	**—**	(19.7)	**—**	(12.6)	**—**	(32.3)
Consolidated	**$ 38.1**	$ 38.6	**$ 23.0**	$ 36.7	**$ 33.6**	$ 32.3	**$ 133.7**	$ 202.4	**$ 228.4**	$ 310.0
Net Earnings Per Share:**										
Continuing	**$ .39**	$ .42	**$ .24**	$ .41	**$ .34**	$ .55	**$ 1.54**	$ 1.24	**$ 2.41**	$ 2.62
Discontinued	**—**	(.02)	**—**	(.04)	**—**	(.01)	**—**	.09	**—**	.02
Gain on Sale of B. Dalton	**—**	—	**—**	—	**—**	—	**—**	.88	**—**	.88
Extraordinary Charge	**—**	—	**—**	—	**—**	(.20)	**—**	(.13)	**—**	(.33)
Consolidated	**$ .39**	$ .40	**$ .24**	$ .37	**$ .34**	$ .34	**$ 1.54**	$ 2.08	**$ 2.41**	$ 3.19
Average Common Shares Outstanding (Millions)	**97.4**	97.2	**97.4**	97.3	**97.2**	97.3	**87.1**	97.4	**94.8**	97.3

*Gross profit is revenues less cost of retail sales, buying and occupancy.

**Earnings per share are computed independently for each of the quarters presented. In 1987, the sum of the quarterly earnings per share does not equal the total-year amount because of the impact of the stock repurchase program on average shares outstanding.

Consolidated Results of Operations

Dayton Hudson Corporation and Subsidiaries

(Millions of Dollars, Except Per-Share Data)	1987	1986	1985
Revenues	**$10,677.3**	$9,259.1	$8,255.3
Costs and Expenses			
Cost of retail sales, buying and occupancy	**7,852.6**	6,705.2	5,908.3
Selling, publicity and administrative	**1,768.8**	1,538.1	1,365.9
Depreciation	**230.9**	182.7	158.2
Rental expense	**97.1**	73.1	69.0
Interest expense, net	**151.8**	117.5	99.8
Taxes other than income taxes	**176.3**	148.3	136.3
	10,277.5	8,764.9	7,737.5
Earnings From Continuing Operations Before Income Taxes and Extraordinary Charge	**399.8**	494.2	517.8
Provision for Income Taxes	**171.4**	239.2	237.3
Net Earnings From Continuing Operations Before Extraordinary Charge	**228.4**	255.0	280.5
Net Earnings From Discontinued Operations:			
Earnings From Operations	—	2.1	3.1
Gain on Sale of B. Dalton	—	85.2	—
Net Earnings Before Extraordinary Charge	**228.4**	342.3	283.6
Extraordinary Charge From Purchase and Redemption of Debt, Net of Tax Benefit	—	(32.3)	—
Consolidated Net Earnings	**$ 228.4**	$ 310.0	$ 283.6
Net Earnings Per Share			
Continuing Operations	**$ 2.41**	$ 2.62	$ 2.89
Discontinued Operations:			
Earnings From Operations	—	.02	.03
Gain on Sale of B. Dalton	—	.88	—
Earnings Before Extraordinary Charge	**2.41**	3.52	2.92
Extraordinary Charge	—	(.33)	—
Consolidated	**$ 2.41**	$ 3.19	$ 2.92
Average Common Shares Outstanding (Millions)	**94.8**	97.3	97.1

These financial statements should be read in conjunction with the Analysis of Continuing Operations on pages 17-21 and the information on pages 26-28.

Dayton Hudson Corporation and Subsidiaries

(Millions of Dollars)	January 30, 1988	January 31, 1987
ASSETS		
Current Assets		
Cash	$ 115.6	$ 64.8
Marketable securities	59.5	159.0
Accounts receivable (net of allowance for doubtful accounts of $28.8 and $29.5)	1,073.5	1,052.5
Merchandise inventories (net of accumulated LIFO provision of $110.4 and $179.5)	1,623.3	1,312.5
Other	36.4	28.6
	2,908.3	2,617.4
Property and Equipment		
Land	439.9	328.3
Buildings and improvements	2,162.5	1,466.3
Fixtures and equipment	1,207.3	959.7
Construction-in-progress	166.5	455.5
Accumulated depreciation	(985.4)	(807.5)
	2,990.8	2,402.3
Property Under Capital Leases, Net	115.0	114.9
Assets Held for Resale	16.5	100.5
Other	44.9	46.9
	$6,075.5	$5,282.0

LIABILITIES AND SHAREHOLDERS' INVESTMENT		
Current Liabilities		
Notes payable	$ 353.3	$ —
Accounts payable (including outstanding drafts of $293.7 and $185.8)	1,054.5	841.9
Accrued liabilities	438.4	429.3
Income taxes - payable and current deferred	121.2	142.7
Current portion of capital lease obligations and long-term debt	18.4	10.7
	1,985.8	1,424.6
Capital Lease Obligations	135.3	131.6
Long-Term Debt	1,683.4	1,244.9
Deferred Income Taxes and Other	285.0	301.4
Shareholders' Investment		
Common stock	85.8	97.4
Additional paid-in capital	22.9	18.4
Retained earnings	1,877.3	2,063.7
	1,986.0	2,179.5
	$6,075.5	$5,282.0

These financial statements should be read in conjunction with the Analysis of Continuing Operations on pages 17-21 and the information on pages 26-28.

Consolidated Statements of Cash Flows

Dayton Hudson Corporation and Subsidiaries

(Millions of Dollars)	1987	1986	1985
Operating Activities			
Net earnings from continuing operations before extraordinary charge	**$ 228.4**	$ 255.0	$280.5
Reconciliation to cash flow:			
Depreciation and amortization	**232.4**	184.9	159.3
Non-current deferred tax provision	**5.8**	39.3	32.0
Current deferred tax provision	**(36.3)**	(1.0)	14.3
(Increase) in accounts receivable	**(21.0)**	(1.7)	(63.0)
(Increase) in inventory	**(310.9)**	(162.5)	(160.4)
Increase in accounts payable	**212.6**	184.9	114.0
Other	**(1.1)**	36.7	40.0
Cash Flow Provided by Continuing Operations	**309.9**	535.6	416.7
Cash Flow Provided by Discontinued Operations	—	50.3	12.2
	309.9	585.9	428.9
Investing Activities			
Expenditures for property	**787.2**	593.8	395.1
Acquisition (disposition) of Target real estate			
Assets held for remodel	—	322.0	—
Assets held for resale	**(75.2)**	100.5	—
Disposals of property	**(11.4)**	(10.1)	(7.8)
Activities of discontinued operations, net	—	(155.2)	21.6
	700.6	851.0	408.9
Net Financing Requirements	**390.7**	265.1	(20.0)
Financing Activities			
Increase in notes payable	**353.3**	—	—
Additions to long-term debt	**450.6**	1,000.0	300.0
Purchase and redemption of debt	—	(558.5)	—
Premium on debt purchase and redemption, net of tax	—	(32.3)	—
Principal payments on long-term debt and capital lease obligations	**(19.2)**	(10.5)	(121.5)
Repurchase of stock	**(339.6)**	—	—
Dividends paid	**(87.5)**	(81.7)	(73.8)
Other	**(15.6)**	(7.9)	(2.7)
	342.0	309.1	102.0
Net (Decrease)/Increase in Cash and Cash Equivalents	**(48.7)**	44.0	122.0
Cash and cash equivalents at beginning of year	**223.8**	179.8	57.8
Cash and cash equivalents at end of year	**$ 175.1**	$ 223.8	$179.8

Amounts in this statement are presented on a cash basis and therefore may differ from those shown in other sections of this annual report.

Investing and financing activities not reported in the Statements of Cash Flows, because they do not involve cash, include capital lease obligations incurred when we entered into leases for buildings and equipment of $8.2 million, $9.1 million and $7.9 million in 1987, 1986 and 1985, respectively. In addition, non-cash capital expenditures resulting from assumed liabilities and asset reclassifications were $43.4 million and $16.0 million in 1987 and 1986, respectively. There were no such transactions in 1985.

Interest paid (including interest capitalized) during 1987, 1986 and 1985 was $141.0, $121.9 and $86.4, respectively. Income tax payments of $217.7, $190.5, and $187.4 were made during 1987, 1986, and 1985, respectively.

The net change in notes payable includes the issuance of $66.0 million and repayment of $60.0 million of commercial paper with maturities over 90 days in 1987 and the issuance and repayment of $16.0 million of commercial paper with maturities over 90 days in 1985. There were no such transactions in 1986.

These financial statements should be read in conjunction with the Analysis of Continuing Operations on pages 17-21 and the information on pages 26-28.

Dayton Hudson Corporation and Subsidiaries

(Millions of Dollars)	Total	Common Stock	Additional Paid-In Capital	Retained Earnings
Balance February 2, 1985	$1,736.5	$ 97.0	$ 9.5	$1,630.0
Consolidated net earnings	283.6			283.6
Dividends declared	(76.2)			(76.2)
Stock option activity	3.5	0.2	3.3	
Balance February 1, 1986	1,947.4	97.2	12.8	1,837.4
Consolidated net earnings	310.0			310.0
Dividends declared	(83.7)			(83.7)
Stock option activity	5.8	0.2	5.6	
Balance January 31, 1987	2,179.5	97.4	18.4	2,063.7
Consolidated net earnings	228.4			228.4
Dividends declared	(87.0)			(87.0)
Stock option activity	4.7	0.2	4.5	
Stock repurchase	(339.6)	(11.8)		(327.8)
Balance January 30, 1988	$1,986.0	$ 85.8	$22.9	$1,877.3

Preferred Stock

Authorized 5,000,000 shares, voting, $.01 par value; no shares outstanding at January 30, 1988 and January 31, 1987.

Common Stock

Authorized 500,000,000 shares $1 par value; 85,775,189 shares issued and outstanding at January 30, 1988; 97,368,703 shares issued and outstanding at January 31, 1987.

Junior Preferred Stock Rights

In September 1986, we declared a distribution of preferred share purchase rights. Terms of the plan provide for a distribution of one preferred share purchase right on each outstanding share of Dayton Hudson common stock. Each right will entitle shareholders to buy one-hundredth of a share of a new series of junior participating preferred stock at an exercise price of $150, subject to adjustment. The rights will be exercisable only if a person or group acquires ownership of 20% or more of Dayton Hudson common stock or announces a tender offer to acquire 30% or more of the common stock.

These financial statements should be read in conjunction with the Analysis of Continuing Operations on pages 17-21 and the information on pages 26-28.

(Millions of Dollars)

Consolidation. Our financial statements include the accounts of Dayton Hudson Corporation and subsidiaries after elimination of material intercompany balances and transactions. All subsidiaries are wholly owned.

Marketable Securities. We record short-term investments at cost, which approximates market.

Sales and Accounts Receivable. Our policy generally is to write off accounts receivable when any portion of the balance is 12 months past due, or when the required payments have not been received for six consecutive months. We base our allowance for doubtful accounts receivable on our past bad debt experience and on the ages of the various accounts.

In 1987, for tax purposes, a bad debt is recognized when the account is written off. In prior years, the reserve method was used to determine bad debt expense.

All customer receivables are classified as current assets, including some which are due after one year. This is consistent with practice in the retail industry.

For financial reporting, we recognize the gross profit on retail installment sales when the sales are recorded. For income tax purposes, we used the installment method of reporting profit on these sales through 1986.

Inventories. Inventories and the related cost of sales are accounted for by the retail inventory method using the last-in, first-out (LIFO) basis. In 1987, certain additional costs are included in inventory for income tax purposes.

Property and Equipment. Property and equipment is recorded at cost less accumulated depreciation. For financial reporting, we compute depreciation on our property using the straight-line method over estimated useful lives. For tax purposes, we generally use accelerated depreciation methods.

Investment Tax Credit. The investment tax credit reduces income taxes in the year we begin using the related property.

Per-Share Data. To compute net earnings per share, we divide net earnings by the weighted average number of common shares outstanding. Performance shares and the exercise of stock options would not materially dilute earnings per share.

Statements of Cash Flows. We adopted the provisions of Statement of Accounting Standards No. 95, "Statement of Cash Flows," in our 1987 financial statements and restated previously reported statements of changes in financial position for 1986 and 1985. For purposes of the statements of cash flows, we consider all short-term investments purchased with a maturity of three months or less to be cash equivalents.

Fiscal Year. Our fiscal year ends on the Saturday nearest January 31:

Fiscal Year	Ended	Weeks
1987	January 30, 1988	52
1986	January 31, 1987	52
1985	February 1, 1986	52

Unless otherwise stated, references to years in this report relate to fiscal years rather than to calendar years.

Lines of Credit

At January 30, 1988, we had $353.3 million in commercial paper outstanding at a weighted average interest rate of 6.9%. During the year, the average amount of commercial paper and notes payable outstanding was $240.1 million at a weighted average interest rate of 7.2%.

We maintain $68.5 million of unsecured lines of credit with nine banks. Borrowings under these lines were at the prime interest rate or at other rates agreed upon at the time of the borrowings. We compensate the banks for the lines of credit through the payment of fees. We were not required to maintain any compensating balances under any of the agreements during 1987.

At year-end we also had additional credit available in the form of four annually renewable, three-year revolving credit agreements: one for $185 million with nine lending institutions, one for $65 million with four lending institutions, and two for $300 million each with two separate lending institutions. Subsequent to year-end, we reduced the two $300 million facilities to $100 million each. We pay a fee for the availability of the revolving credit agreements and have the option of borrowing at the prime rate or other negotiated rates. During 1987, we paid fees of $1.1 million under these agreements. Any balance outstanding under the remaining agreements at the end of a three-year period may be converted at our option into a four-year term loan. There were no balances outstanding at January 30, 1988.

Between September 15 and December 18, 1987, we maintained additional unsecured bank lines of credit ranging from $78 to $328 million to meet seasonal working capital needs.

Long-Term Debt

During 1987, we issued $150 million of 9⅞% sinking fund debentures due 2017, $50 million of 9.20% notes due 1991, and $50 million of 9.39% notes due 1992. We also issued $200.6 million of notes with interest rates of 8.05% to 9.35% and maturity dates of 1990 to 1993. The additional debt was used for capital expansion and store remodeling and to finance the stock repurchase program. We also assumed $10.5 million of mortgage notes with interest rates of 9.25% due 2003 and 2004 in connection with the acquisition of real estate.

At year-end 1987 and 1986, long-term debt due beyond one year was:

	Jan. 30, 1988	Jan. 31, 1987
8.05% to 9⅞% Notes and Sinking Fund Debentures due 1990 to 2017	**$ 450.6**	$ —
7½% to 14¾% Unsecured and Sinking Fund Notes and Debentures due 1992 to 2016	**1,164.4**	1,180.0
7¾% to 13¼% Other Unsecured Notes Due 1990 to 2014	**38.1**	38.5
6½% to 14% Notes and Contracts for purchase of real estate due 1992 to 2010	**30.3**	26.4
Total	**$1,683.4**	$1,244.9

The sinking fund and principal payments on this long-term debt over the next five years will be $14.0 million in 1988, $97.0 million in 1989, $51.7 million in 1990, $193.0 million in 1991 and $83.0 million in 1992.

Subsequent Debt Issues. Subsequent to fiscal year-end, we issued $100 million of 9⅝% debentures due 2008 and $22.5 million of 8.4% to 9.0% notes due 1992 to 1995.

Covenants and Collateral. In most of our long-term debt agreements, as well as the revolving credit agreements, we have agreed to observe certain covenants at the request of the lenders. Among these are restrictions related to levels of working capital, funded debt, dividends and secured debt, as well as change of control. Under the most restrictive of these provisions, $1.18 billion of our retained earnings at the end of 1987 was available for dividends and other types of restricted payments.

As a condition of borrowing under our mortgage notes and contracts, we have pledged related land, buildings and equipment as collateral. At year-end, approximately $46.0 million of our property and equipment served as collateral for these loans.

Leases

For financial reporting, we classify leases as either operating or capital leases. Capital leases are recorded as assets in our Statements of Financial Position and we report interest and depreciation expense on the leases instead of rent expense. Operating leases are not capitalized and lease rentals are expensed. For tax purposes, we deduct rent expense on all leases.

Many of our longer-term leases include options to renew, with renewal terms varying from five to thirty years. Certain leases also include options to purchase the property. In addition, we have leases on equipment with remaining terms ranging from one to five years.

The detail of leased property and equipment which we have capitalized in our Statements of Financial Position is:

	Jan. 30, 1988	Jan. 31, 1987
Land and buildings	**$168.8**	$162.1
Equipment	**12.8**	12.0
Accumulated depreciation	**(66.6)**	(59.2)
Net	**$115.0**	$114.9

If we were to capitalize the minimum lease payments for all of our operating leases with initial terms of over one year, the present value of these payments would be approximately $376.1 million at year-end 1987 and $382.2 million at year-end 1986. These present values were calculated using an average interest rate for each lease based on the year of inception. The weighted average interest rate used to calculate the 1987 present value was 11% compared with 12% for 1986.

The impact of recording depreciation and interest expense rather than rent expense on the capital leases has been to decrease our net earnings by $1.7 million in 1987, $1.7 million in 1986, and $1.8 million in 1985. Capital lease depreciation expense was $8.0 million in 1987, $8.1 million in 1986, and $8.0 million in 1985.

Rent expense includes percentage rents which are based on a percentage of sales over stated levels. Executory costs included in our rental payment or charged in addition to rent are excluded from rent expense and are included in occupancy costs in our Results of Operations.

Composition of Rental Expense	**1987**	1986	1985
Minimum rents on long-term operating leases	**$71.1**	$51.9	$46.3
Short-term rents	**13.8**	9.3	9.4
Percentage rents:			
Operating leases	**14.2**	13.9	14.6
Capital leases	**1.6**	1.3	1.2
Sublease income	**(1.9)**	(1.7)	(1.0)
Executory costs	**(1.7)**	(1.6)	(1.5)
Net expense	**$97.1**	$73.1	$69.0

Future minimum lease payments which must be made under noncancellable lease agreements existing at the end of 1987 are:

	Operating Leases	**Capital Leases**
1988	$ 66.6	$ 21.8
1989	62.8	21.7
1990	61.5	21.6
1991	60.9	21.2
1992	60.7	20.4
After 1992	504.1	265.8
Total minimum lease payments (a)	$816.6	$372.5
Less: Interest		223.3
Executory costs		9.5
Capitalized lease obligations, including current portion of $4.4		$139.7

(a) Minimum rental payments have not been reduced by minimum sublease rentals due in the future under noncancellable subleases ($7.3 million for operating leases, $10.9 million for capital leases).

Commitments and Contingencies

Commitments for the purchase of real estate, construction of new facilities and remodeling amounted to approximately $110.5 million at January 30, 1988. We had additional commitments of $41.9 million for equipment purchases.

Our contingent liability for mortgage debt on certain office properties sold in 1976 and certain shopping centers sold in 1978 was approximately $34.3 million at January 30, 1988. The purchasers have agreed to indemnify us for any costs we might incur in relation to the mortgages.

Our business brings us into regular contact with the general public, other businesses and governmental entities. This contact subjects us to claims and litigation arising out of the ordinary course of business. Considering the insurance coverage in place for a portion of the claims and litigation, and noting that the ultimate consequences cannot be accurately predicted, management and legal counsel believe that presently identified claims and litigation will not have a material adverse effect on our operations or financial condition.

(Millions of Dollars)

Pension Plans

We have three defined benefit pension plans which cover all employees who meet certain requirements of age, length of service and hours worked per year. The benefits provided are based upon years of service and the employee's compensation during the last five years of employment.

Contributions to the pension plans, which are made solely by the Corporation, are determined by our outside actuarial firm. To compute net pension cost, our actuarial firm estimates the total benefits which will ultimately be paid to eligible employees and then allocates these costs to service periods. Assumptions are made on the years the employees will work, their future salary increases, the number of employees who will earn the right to receive benefits under the plans, the rate at which future pension benefits should be discounted and the rate of return which will be earned on the plans' present assets and future contributions.

During 1985, we changed our method of accounting for pension costs to comply with the Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions." Service cost is computed by determining the increase in future pension benefits resulting from the current year's service and discounting these future cash flows to the present. The projected benefit obligation is the actuarial present value of all future benefit payments for services rendered to date, including an assumption for future compensation levels.

The period over which unrecognized pension costs and credits are amortized, including prior service costs and actuarial gains and losses, is based on the remaining service period for those employees expected to receive pension benefits. Actuarial gains and losses result when actual experience differs from that assumed or when actuarial assumptions are changed.

The following tables reflect consolidated pension amounts.

Components of Net Pension Credit	**1987**	1986	1985
Service cost–benefits earned during the period	**$ 10.8**	$ 9.0	$ 8.6
Interest cost on projected benefit obligation	**18.7**	17.5	16.6
Return on assets–actual	**(22.5)**	(39.1)	(44.9)
–deferred	**(0.7)**	17.5	24.3
Amortization of transitional asset	**(8.0)**	(8.0)	(7.9)
Net pension (credit)	**$ (1.7)**	$ (3.1)	$ (3.3)

	December 31,	
Funded Status	**1987**	1986
Actuarial present value of:		
Vested benefit obligation	**$186.1**	$183.0
Accumulated benefit obligation	**$195.8**	$193.2
Projected benefit obligation	**$222.7**	$221.3
Fair market value of plan assets *	**281.0**	276.1
Plan assets in excess of projected benefit obligation	**58.3**	54.8
Unrecognized prior service cost	**.8**	—
Unrecognized net actuarial gain	**(22.4)**	(15.8)
Unrecognized transitional asset	**(31.0)**	(39.0)
Prepaid pension asset	**$ 5.7**	$ —

*Plan assets consist primarily of equity securities and fixed income securities.

	December 31,		
Actuarial Assumptions	**1987**	1986	1985
Discount rate	**9.0%**	8.5%	9.5%
Expected long-term rate of return on plan assets	**9.5**	9.5	9.5
Average assumed rate of compensation increase	**6.9**	6.9	6.9

Postretirement Health Care Benefits

In addition to providing pension and other supplemental benefits, we provide certain health care benefits for our retired employees. Employees become eligible for these benefits if they meet minimum age and service requirements, are eligible for retirement benefits and agree to contribute a portion of the cost. We have the right to modify these benefits. The cost of providing these retiree health care benefits is recognized as expense when claims are paid. These costs amounted to approximately $2.0 million, $1.7 million and $1.7 million for 1987, 1986 and 1985, respectively.

Stock Options and Performance Shares

We have two stock option plans for key employees. Grants have included stock options, performance shares or both. The options have included Incentive Stock Options, Non-Qualified Stock Options or a combination of both. Twelve months after the grant date, 25% of any options granted become exercisable with another 25% after each succeeding 12 months. The options are cumulatively exercisable and expire no later than 10 years after the date of the grant. The performance shares pay cash and stock if certain selected performance goals are met at the end of a four-year period.

We record compensation expense on performance shares based on current market price of our common stock and the extent to which the performance goals are being met. We recorded expense of $0.4 million, $0.9 million and $1.4 million in 1987, 1986 and 1985, respectively. When employees exercise options, the total option price is credited to Common Stock and Additional Paid-in Capital, and no expense is incurred.

The number of shares of unissued common stock reserved for future grants under all the plans was 4,373,123 at the end of 1987 and 4,569,142 at the end of 1986.

		Options		
Options and Performance Shares Outstanding	Number of Shares	Price Per Share	Shares Exercisable	Performance Shares
1985				
Beginning of year	1,238,165	$ 4.52-$37.34	689,192	134,109
Granted	340,761	39.94		
Cancelled	(34,121)	14.30- 39.94		
Exercised	(186,656)	4.52- 37.34		
1986				
Beginning of year	1,358,149	7.13- 39.94	698,955	100,714
Granted	121,361	53.19		
Cancelled	(53,333)	17.44- 53.19		
Exercised	(167,492)	7.13- 39.94		
1987				
Beginning of year	1,258,685	8.70- 53.19	767,640	85,411
Granted	243,535	30.25- 53.25		
Cancelled	(91,994)	33.88- 53.19		
Exercised	(216,077)	8.70- 53.19		
End of year	1,194,149	$ 9.31-$53.25	713,808	116,272

Report of Ernst & Whinney, Independent Auditors

Board of Directors and Shareholders
Dayton Hudson Corporation
Minneapolis, Minnesota

We have examined the consolidated statements of financial position of Dayton Hudson Corporation and subsidiaries as of January 30, 1988 and January 31, 1987, and the related consolidated statements of results of operations, cash flows and shareholders' investment for each of the three years in the period ended January 30, 1988. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the consolidated financial position of Dayton Hudson Corporation and subsidiaries at January 30, 1988 and January 31, 1987 and the consolidated results of their operations for each of the three years in the period ended January 30, 1988, in conformity with generally accepted accounting principles applied on a consistent basis.

Ernst & Whinney

Minneapolis, Minnesota
March 18, 1988

Responsibility for Financial Statements and Accounting Controls

The financial statements and other information presented in this report have been prepared in accordance with generally accepted accounting principles. Management is responsible for the consistency, integrity and presentation of the information in the Annual Report, which necessarily includes some amounts based upon our judgments and best estimates.

To discharge this responsibility, we maintain comprehensive systems of internal controls designed to provide reasonable assurance that assets are safeguarded and transactions are executed in accordance with established procedures. The concept of reasonable assurance is based upon a recognition that the cost of the controls should not exceed the benefit derived. After judging the cost and benefit factors, we believe our systems of internal controls provide this reasonable assurance.

The Audit Committee of the Board of Directors, consisting of five outside directors, recommends independent auditors for appointment by the Board, and reviews their proposed services and their reports. The Committee also reviews the internal audit plan and their audit reports. Our independent auditors, Ernst & Whinney, our internal auditors and our corporate controller have full and free access to the Audit Committee, and meet with it periodically, with and without the presence of management. The results of the auditors' examinations and their opinions on the adequacy of our internal controls and the quality of our financial reporting are regularly reviewed by the Committee.

Our financial statements have been examined by Ernst & Whinney, whose report appears on this page. Their report expresses an opinion as to the fair presentation of the financial statements and is based on an independent examination made in accordance with generally accepted auditing standards.

Kenneth A. Macke
Chairman of the Board and
Chief Executive Officer

Bruce G. Allbright
President

Willard C. Shull, III
Senior Vice President,
Finance

Ralph W. Salo
Senior Vice President,
Control

Financial Comparisons

Dayton Hudson Corporation and Subsidiaries

(Millions of Dollars, Except Per-Share Data)	1987	1986	1985	1984(a)	1983	1982	1981	1980	1979	1978(a)	1977
Revenues	**$10,677.3**	9,259.1	8,255.3	7,519.2	6,518.2	5,286.4	4,623.6	3,777.9	3,174.9	2,787.5	2,356.7
Cost of retail sales, buying and occupancy	**$ 7,852.6**	6,705.2	5,908.3	5,392.1	4,642.5	3,721.7	3,278.3	2,678.7	2,218.1	1,943.7	1,643.8
Selling, publicity and administrative	**$ 1,768.8**	1,538.1	1,365.9	1,234.4	1,080.5	901.8	826.9	690.1	590.4	508.5	417.9
Depreciation	**$ 230.9**	182.7	158.2	144.9	123.1	99.4	85.1	62.4	46.8	37.5	34.1
Interest expense, net	**$ 151.8**	117.5	99.8	97.7	86.1	64.9	47.1	13.6	5.4	14.2	15.1
Earnings From Continuing Operations Before Income Taxes and Extraordinary Charge	**$ 399.8**	494.2	517.8	453.5	415.9	358.1	261.2	230.0	223.0	183.7	173.7
Income Taxes	**$ 171.4**	239.2	237.3	207.9	189.1	165.6	116.2	103.1	106.8	95.1	88.8
Net Earnings											
Continuing	**$ 228.4**	255.0	280.5	245.6	226.8	192.5	145.0	126.9	116.2	88.6	84.9
Discontinued (b)	**$ —**	87.3(c)	3.1	13.7	18.7	14.2	28.4	19.8	75.9(d)	176.3(d)	13.0
Extraordinary charge	**$ —**	(32.3)	—	—	—	—	—	—	—	—	—
Consolidated	**$ 228.4**	310.0	283.6	259.3	245.5	206.7	173.4	146.7	192.1	264.9	97.9
Per Common Share											
Net earnings											
Continuing	**$ 2.41**	2.62	2.89	2.54	2.35	2.00	1.51	1.33	1.23	.93	.91
Discontinued (b)	**$ —**	.90(c)	.03	.14	.19	.15	.30	.21	.80(d)	1.87(d)	.13
Extraordinary charge	**$ —**	(.33)	—	—	—	—	—	—	—	—	—
Consolidated	**$ 2.41**	3.19	2.92	2.68	2.54	2.15	1.81	1.54	2.03	2.80	1.04
Cash dividend declared	**$ .945**	.86	.785	.695	.625	.575	.525	.475	.425	.375	.325
Shareholders' investment	**$ 23.15**	22.38	20.04	17.90	15.91	13.98	12.41	11.14	10.09	8.50	6.10
Return on Beginning Equity (Shareholders' Investment)											
Continuing	**10.5%**	13.1	16.2	15.9	16.8	16.1	13.6	13.2	14.4	15.3	17.0
Consolidated	**10.5%**	15.9	16.3	16.8	18.2	17.3	16.3	15.2	23.8	45.7	19.6
Capital Expenditures	**$ 838.8**	940.9	403.0	336.1	320.7	268.2	238.1	247.2	201.8	147.9	100.4
Consolidated Year-End Financial Position											
Working capital	**$ 922.5**	1,192.8	1,130.2	972.8	868.6	718.3	508.9	381.3	438.8	427.6	309.4
Property and equipment, net	**$ 2,990.8**	2,402.3	1,655.7	1,418.6	1,306.8	1,139.0	978.1	826.7	596.3	451.0	363.6
Property under capital leases, net	**$ 115.0**	114.9	114.7	114.7	115.8	97.9	93.9	100.4	67.2	70.9	57.0
Total assets	**$ 6,075.5**	5,282.0	4,417.5	3,799.9	3,594.9	2,985.3	2,555.2	2,155.2	1,793.2	1,637.5	1,411.4
Long-term capital lease obligations	**$ 135.3**	131.6	128.1	125.2	123.9	102.4	96.3	103.3	73.0	76.8	62.0
Long-term debt	**$ 1,683.4**	1,244.9	794.5	625.4	626.8	529.3	331.8	213.8	117.6	94.3	116.8
Shareholders' investment	**$ 1,986.0**	2,179.5	1,947.4	1,736.5	1,540.2	1,348.8	1,192.7	1,066.4	962.6	808.4	579.8
Average Common Shares Outstanding (Millions)	**94.8**	97.3	97.1	96.9	96.6	96.2	95.8	95.2	94.8	94.4	94.0

The Financial Comparisons should be read in conjunction with the Financial Statements.

Per-share amounts and shares outstanding reflect two-for-one common stock splits effective July 1983 and November 1981.

(a) Consisted of 53 weeks.

(b) Discontinued operations include discontinued real estate for 1977-1981 and B. Dalton Bookseller for 1977-1986.

(c) Includes the gain on sale of B. Dalton Bookseller.

(d) Includes gains on sale of real estate.

Directors

Bruce G. Allbright
President

Rand V. Araskog
Chairman of the Board and Chief Executive Officer, ITT Corporation (diversified multinational company) (1)(3)(5)

Robert A. Burnett
Chairman and Chief Executive Officer, Meredith Corporation (media company engaged in printing, publishing, broadcasting and real estate) (1)(2)(3)

Livio D. DeSimone
Executive Vice President, 3M Company (diversified manufacturer) (1)(2)(4)

Roger L. Hale
President and Chief Executive Officer, Tennant Company (industrial equipment manufacturer) (1)(3)(5)

Donald J. Hall
Chairman of the Board, Hallmark Cards, Incorporated (greeting card manufacturer) (1)(2)(3)

Betty Ruth Hollander
Chairman of the Board and Chief Executive Officer, The Omega Group, Inc. (manufacturer of scientific measurement and control devices and systems, technical publishing and industrial and commercial real estate development) (1)(2)(4)

David T. Kearns
Chairman and Chief Executive Officer, Xerox Corporation (business products and systems, and financial service business) (1)(3)(5)

Kenneth A. Macke
Chairman of the Board and Chief Executive Officer (1)

Bruce K. MacLaury
President, The Brookings Institution (research and education organization) (1)(4)(5)

David T. McLaughlin
Chairman, The Aspen Institute for Humanistic Services (institute for discussion of contemporary issues) (1)(4)(5)

John A. Rollwagen
Chairman of the Board and Chief Executive Officer, Cray Research, Inc. (manufacturer of super computers) (1)(2)(4)

(1) Executive Committee
(2) Audit Committee
(3) Compensation Committee
(4) Corporate Responsibility Committee
(5) Finance Committee

Officers

Kenneth A. Macke*
Chairman of the Board and Chief Executive Officer

Bruce G. Allbright*
President

James T. Hale*
Senior Vice President and Secretary

Ralph W. Salo*
Senior Vice President

Willard C. Shull, III*
Senior Vice President

Edwin H. Wingate*
Senior Vice President

Ann H. Barkelew*
Vice President

Larry E. Carlson
Vice President

Karol D. Emmerich*
Vice President and Treasurer

L. Fred Hamacher
Vice President

William E. Harder
Vice President and Assistant Secretary

Peter C. Hutchinson*
Vice President

Kathy Barnes Probelski
Vice President

James R. Eckmann
Assistant Treasurer

William P. Hise
Assistant Secretary

Operating Company Management

Target
Robert J. Ulrich*
Chairman and Chief Executive Officer

Mervyn's
Walter T. Rossi*
President and Chief Executive Officer

Dayton Hudson Department Store Company
Stephen E. Watson*
Chairman and Chief Executive Officer

Raj Joneja
President

Lechmere
C. George Scala*
Chairman, President and Chief Executive Officer

*Executive Officers

Stores and Locations

Target

	No. of Stores	Retail Sq. Ft. (000)
Arizona	12	1,244
Arkansas	3	289
California	91	9,437
Colorado	17	1,761
Illinois	5	407
Indiana	31	2,583
Iowa	16	1,320
Kansas	2	200
Kentucky	5	427
Louisiana	2	202
Michigan	6	630
Minnesota	21	2,384
Missouri	11	1,137
Montana	2	182
Nebraska	4	406
Nevada	5	501
North Dakota	4	364
Ohio	1	79
Oklahoma	8	783
South Dakota	2	201
Tennessee	9	886
Texas	48	4,904
Wisconsin	10	1,109
Wyoming	2	182
	317	31,618

Major Markets	No. of Stores
Los Angeles/Orange County	47
Minneapolis/St. Paul	18
Houston	15
Dallas/Fort Worth	14
Denver	12
San Francisco Bay Area	12

Mervyn's

	No. of Stores	Retail Sq. Ft. (000)
Arizona	11	906
California	93	7,152
Colorado	8	648
Georgia	6	476
Louisiana	7	538
Michigan	8	612
Nevada	6	422
New Mexico	2	180
Oklahoma	3	270
Oregon	6	505
Texas	36	2,867
Utah	6	530
Washington	7	621
	199	15,727

Major Markets	No. of Stores
Los Angeles/Orange County	36
San Francisco Bay Area	18
Dallas/Fort Worth	12
Houston	9
San Diego	7
Detroit	6
Phoenix	6

Dayton Hudson Department Store Company

	No. of Stores	Retail Sq. Ft. (000)
Hudson's		
Indiana	2	246
Michigan	17	4,180
Ohio	1	187
	20	4,613
Dayton's		
Minnesota	12	2,676
North Dakota	3	299
South Dakota	1	102
Wisconsin	1	101
	17	3,178
	37	7,791

Major Markets	No. of Stores
Minneapolis/St. Paul	10
Detroit	8

Lechmere

	No. of Stores	Retail Sq. Ft. (000)
Connecticut	1	77
Florida	2	136
Georgia	4	348
Massachusetts	8	947
New Hampshire	2	204
New York	4	349
North Carolina	1	77
Rhode Island	2	179
	24	2,317

Major Markets	No. of Stores
Boston	6
Atlanta	4

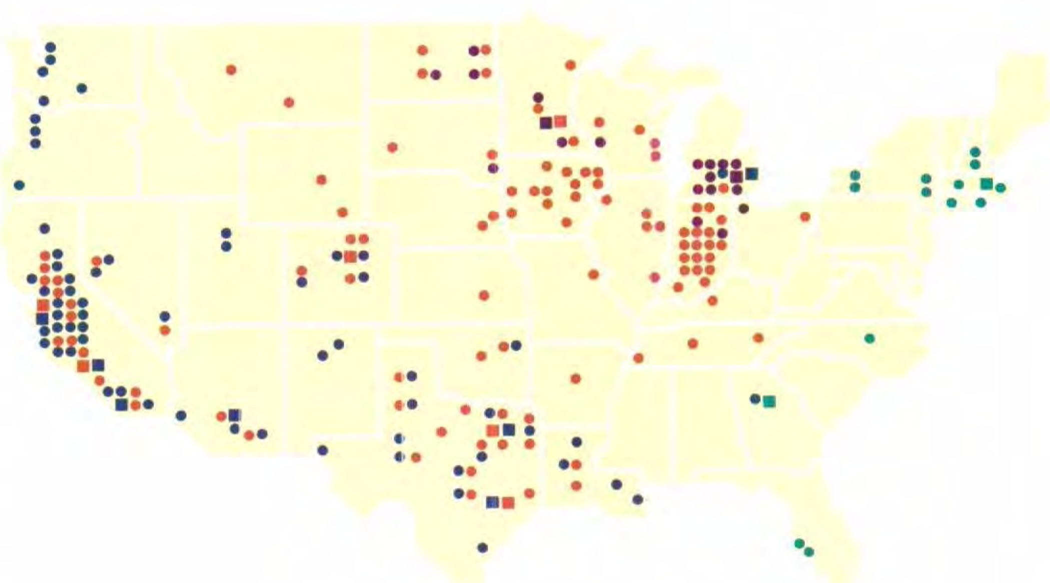
□ Major Markets ○ Other Cities

Target

Mervyn's

Dayton Hudson Department Store Company

Lechmere



Total All Stores	577
Total Retail Square Feet	57,453

Corporate Information

Corporate Offices

777 Nicollet Mall, Minneapolis,
Minnesota 55402
Telephone: (612)370-6948

Annual Meeting

The Annual Meeting of Shareholders is scheduled for 9:30 a.m. Wednesday, May 25, 1988, at The Children's Theatre, Minneapolis Institute of Arts, 2400 Third Avenue South, Minneapolis, Minnesota. Shareholders unable to attend can listen to the proceedings live between 9:30 and 10:30 a.m., CDT, by dialing 1-900-590-7676. A tape of the meeting also will run every hour on the hour beginning at 1:00 p.m., CDT. The cost to call is $.45 for the first minute and $.35 for each additional minute. Callers who are not AT&T subscribers must dial the AT&T access code (10288) before dialing the 900 number.

Community Involvement

In keeping with its commitment to corporate responsibility, Dayton Hudson annually contributes an amount equal to 5% of its normalized federally taxable income to support its giving programs. In 1987, we contributed more than $19 million in the communities where we do business. Giving programs were focused in two areas: social action and the arts. For a complete report on 1987 contributions and programs, write to Vice President, External Affairs at the Dayton Hudson corporate offices.

10-K Report

A copy of the Form 10-K annual report filed with the Securities and Exchange Commission for Dayton Hudson's fiscal year ended January 30, 1988, is available at no charge to shareholders. Write to Director, Financial Relations at the Dayton Hudson corporate offices.

Dividend Reinvestment Plan

The dividend reinvestment plan is a convenient way for Dayton Hudson shareholders to acquire additional shares of the Corporation's common stock through automatic dividend reinvestment and voluntary cash purchase. All holders of Dayton Hudson common stock may participate. For more information, write to Morgan Shareholder Services Trust Company, P.O. Box 3506, Church Street Station, New York, New York 10008-3506.

Transfer Agent, Registrar and Dividend Disbursing Agent

Morgan Shareholder Services
Trust Company

Trustee

First Trust National Association

Stock Exchange Listings

New York Stock Exchange
Pacific Stock Exchange
(Trading Symbol DH)

Shareholder Assistance

For assistance regarding individual stock records and transactions, write to Shareholder Relations at the Dayton Hudson corporate office, or telephone the special shareholder information hotline (1-800-338-8053). You also can contact Morgan Shareholder Services Trust Company, P.O. Box 3981, Church Street Station, New York, New York 10008-3981. Information Center telephone: (212)587-6515.

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DAYTON HUDSON CORPORATION

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Minneapolis
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